History of Ideas and Modern Economic Theory

Some Lessons of *Higgling*

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The 1994 annual supplement to *History of Political Economy* has a quality that many history of economics books often lack: it shows how the discipline can contribute to a better understanding of modern economic theory and subsequently enrich it. This perspective is well expressed in Neil De Marchi's and Mary Morgan's introductory statement: "Economics knows two traditions with respect to market transactions. One has grown out of a concern for fairness, the other, for efficiency. In the conventional history of the discipline, economics . . . focused on elucidating the laws governing exchange and efficient allocation. In the process, questions of fairness were pushed out to the margins" (p. 1). By clarifying the relationships between economics and ethics and by examining the development of bargaining and contract theories from this perspective, *Higgling* sheds new light on the current orientations, accomplishments and failures of such theories.

The editors' purpose is to show that higgling deserves the interest and scrutiny of economists. The most obvious justification for that is the fact that "in modern economic theory higgling is not regarded as a relevant activity (Hutter, p. 94), although, as Anne Mayhew observes, 'economists do ... appear to treat something very like the process of higgling when they deal with strategic uncertainty in game theory' (p. 300). Likewise, when turning to the past, one finds that "the notion of higgling has not been central to discourses on the market" (Brown, p. 67). So it appears that the place of higgling in modern economics or, more generally, in the history of economics is not yet clearly defined. Accordingly, this book should help economists to understand why higgling has long remained an unnoticed notion. More importantly, *Higgling* provides another perspective on a number of issues which have experienced a theoretical renewal in recent years. For instance, issues of language and rhetoric have been on the agenda of economists for some years now. Given that persuasion is considered essential in economic contexts, studying higgling, as "use of language in order to effect advantageous transactions" (Brown, p. 66), may be informative to those who believe that rhetoric plays a significant role in economic situations.

Nevertheless, persuasion may involve a wide range of means, some of which are reprehensible. Consequently, higgling may also relate to "opportunism" à la Williamson. Since the 1970s, self-interest seeking with guile has become more familiar to economists. In so far as higgling can involve reprehensible means of persuasion, it can surely provide a better understanding of the phenomenon of "opportunism".

Besides self-interest, only laws, conventions or rules can prevent economic agents from behaving dishonestly. This suggests that institutions should be lent more weight—a fact

that economists seem more willing to accept today than they were two decades ago. In stressing the fact that the market is a social construct characterised by conventions, rules and norms, this volume not only refines our understanding of the process of higgling, but it also exemplifies the special treatment institutions should be given in economics.

Finally, by comparing the notions of higgling in economics with those developed in other social sciences, this book shows that interdisciplinary approaches can reveal new orientations of research and subsequently enrich the economists' understanding of higgling. From this perspective, *Higgling* provides an original contribution to the current attempts at redefining the boundaries between economics, sociology, psychology and anthropology.

Higgling and Language

In their introduction, De Marchi and Morgan emphasize three meanings of higgling. The first two senses are developed by Brown who distinguishes between higgling as the materialisation of some fact in market exchange ratios and higgling as an attempt to change the objective conditions of the market to one's advantage. Hutter provides the third definition. He "argues that higgling is the noise of markets in action" (p. 9). In addition, authors mention definitions from authoritative dictionaries. Brown, for example, quotes the *Oxford English Dictionary*, where "the word *higgling* refers to the notion of close bargaining, cavilling or disputing about terms in market transactions, and itinerant dealing in provisions and petty commodities" (p. 66). Likewise, Margaret Schabas reveals "the most central meaning, which the word [higgle] shares with its older synonym *haggle"*, that is: 'to engage in close bargaining over the terms of an exchange, to dispute a contract' (p. 119). It is interesting to note that no significant distinction is made between higgling and haggling (see p. 66n, 343n), although a higgler is generally bent on raising the price, whereas a haggler (the buyer) is bent on lowering it" (p. 120).

The above definitions give a broad understanding of higgling. However, economists may take liberties with accepted definitions, advocating idiosyncratic concepts of higgling. Brown thus argues that the concept of higgling varies with analytical contexts (concepts of the market or notions of competition, for instance) and that such variations can be traced to different conceptions of language in economics. Part of her argument is centered on the rhetorical techniques used in the marketplace. Brown shows that in the eighteenth century persuasion involved a rather despised form of discourse in comparison with other forms designed to convince through proper and balanced arguments. Therefore, using rhetorical techniques while higgling amounted to using an inferior, indeed disparaged, form of discourse.

Once acknowledged that language is crucial for all discourse, Brown argues, one can challenge the set of classical oppositions between philosophy and rhetoric, truth and falsehood, necessity and contingency, and therefore go beyond the two above mentioned meanings of higgling. From this point of view, the behavior of economic agents is seen as determining competitive outcomes in the sense that it participates actively in constituting the market. More specifically, economic agents turn into economic subjects who, striving to adjust to objective economic facts, change them in a way that may in turn influence their behavior.

One should not underestimate Brown's remarks that a different conception of higgling is possible, as they have important implications for modern economic theory in general and game theory in particular. As for the former, it is clear that regarding the market as a social construct may well change the customary view of the relations of economic agents to institutions in such a way that methodological individualism would need to be amended. Concerning game theory, one can easily understand that taking into account strategic higgling

may entail some form of inquiry into the way economic agents come to know about each other. In a recent book, Binmore (1994) has pointed to the role of empathy in such a process. It appears that empathy may serve the purpose of those economic agents who, willing to deceive others, try to figure out their preferences and accordingly predict their behavior.

Higgling and Opportunism

Higgling resembles many other notions which for variable reasons have fallen into oblivion. Among such notions, "opportunism," as envisaged by Williamson, is of particular importance since the discussion of the conditions of exchanges may involve forms of deception, lying and the like. It comes as no surprise, then, to find higgling closely related to opportunism. Moreover, the fact that both notions have long been ignored by historians of economics is a witness of their association.

S. Todd Lowry shows that even the Greeks, who acknowledged the importance of the volitional aspect of transactions as a guarantee of mutual benefit in exchange, were aware that "one party may have benefited excessively compared to the other" (p. 34). From modern economic theory viewpoint, the answer to Lowry' s question "Can one be voluntarily unjust to oneself?" seems obvious. No! Agents cannot be voluntarily unjust to themselves since they often voluntarily agree on incomplete contracts and therefore know that they may face situations harmful to their own interests. Yet the above question is much more complicated than it appears at first glance, since an economic agent may use opportunistically the incompleteness of the contract to take advantage of another agent. In other words, the idea that "one could not, by definition, voluntarily commit an injustice to oneself" (p. 36), as Lowry put it, presupposes that although one does not and cannot systematically go into the details of the contract, one agrees on it assuming that the other party will respect "normal" business practice.

On this score, the example of the short selling of shares in seventeenth-century Holland makes it clear that the fairness issue always refers to conventions that define what is normal and what is not in a specific marketplace. Neil De Marchi and Paul Harrison remark that "in the first half of the seventeenth century Antwerp merchants who were members of the expatriate colony of traders in Seville applied a special name to interlopers who ignored the conventions of reputation, networks of agents, mutual financing, and so on" (p. 59). Clearly, authors such as Cantillon, Turgot and Smith insisted that the knowledge of market characteristics was not an easy task and that being familiar with a marketplace did not mean being familiar with all marketplaces. Paradoxically, this may explain why these authors did not consider "opportunism" a central issue. As long as markets put together people who know each other— small communities of exchangers — the chance for some of them to behave dishonestly is low. Only strangers to a marketplace can reasonably be expected to behave opportunistically; only strangers who are unaware of the conventions in use in a marketplace can be subject to opportunism. Otherwise, normal business practice prevails.

In a different context, Margaret Schabas shows that by the middle or end of the eighteenth century, higgling declined. With the development of commercial society, one might suspect, transactions in the marketplace gathered more and more people who did not know each other. It is understandable, then, that assessing the others' character became of greater importance than higgling itself. As Schabas observes, "shopping, at least among the well-to-do, was effectively a process of assessing trust and 'good character'" (p. 121). Modern economic theorists are well aware that trust is essential for economic transactions to emerge, persist and develop (see Gambetta 1988). When people transact in markets with which they are familiar, trust can be assured through personal relations. With the spread of commerce, such a situation is less and less frequent and it can be extremely costly for agents to acquire

knowledge about the characteristics of their potential partners. Focusing on Hume, Schabas shows that instead of providing a solution to the problem of assessing trust and good character, Hume stressed promise-keeping in economic transactions and claimed that a moneyed and market economy may urge agents to behave honestly.

Of course, Hume's solution to "opportunism" is not the only one. For example, one may recall John Bates Clark, who believed that "the 'bargain' is an exchange at some price other than market price, in which one party makes no gain, or gets less value than he gives, thus sustaining a loss relative to the exchange in the open market at the market price" (p. 233). According to Clark, Morgan observes, economic laws do not suffice to ensure mutual advantage in exchange. The moral sense of individuals is also needed to restrict exploitative behavior (p. 239). Ross Emmett put forward a similar argument when he characterises Frank Knight's position on exchange behavior. He notes that "good sports are distinguished from other players by the moral quality of their play, which balances the personal interest in winning the game with the social interest in continuing it" (p. 278). However, in modern economics the institutional solution to opportunism has prevailed over the moral one.

Higgling and Institutions

There has been a long tradition in economic thought to emphasize the institutional context of transactions. However, such tradition has never been prominent in mainstream economics. In the twentieth century, it has concerned mainly American institutionalists Investigating the work of Veblen and Commons, Malcolm Rutherford claims that both authors see markets in a broadly similar way, the former by presenting markets as the outcome of "the operation of business principles and practices" (p. 255), the latter by insisting that "bargaining transactions take place within an evolving context of law" (p. 267). Both Veblen and Commons favoured the conception of market as a social construct, as opposed to the standard view of market as a given allocative device. Similarly, Lowry argues that contrary to what one might conclude from the customary conceptualisation of markets, it was only after certain conditions were met (after the Industrial Revolution), that "market processes could be considered superior to the informed rational judgment of responsible magistrates and policy makers" (p. 44). This is a significant observation as it illustrates that in order for markets to be allocatively efficient, other institutions, such as law, social conventions and ethical norms must be present. However, as Philip Mirowski explains while presenting the views of anthropologists, institutions can also impede higgling, only allowing it for the situations "when one is dealing with the truly foreign" (p. 335), whereas, once transactions take place on a regular basis, there is a tendency to favour balanced reciprocity.

Of course, the idea that social conventions can determine the conditions of fair exchange is not foreign to economics. Robert Leonard recounts how Roth and his team reach the conclusion that there is a "sociological hypothesis" about experimental bargaining in the case of intermediate information. As Leonard put it, "Higglers will tend to settle on the focal point of 'fair allocation,' that is, equal expected value of rewards, when the prizes are expressed in terms of 'familiar quantities,' namely, quantities to which social conventions apply, such as money. Once one is dealing in terms of some unfamiliar quantity such as chips, social norms concerning fair division are no longer binding" (p. 354). Without the institution of money, bargainers would experience difficulty in assessing the fairness of a division. Thanks to money the expression of value becomes a conventional language that allow higglers to make interpersonal comparison of wealth.

It is no accident, then, that rediscovering the role of institutions in a market economy, economists would again come to grips with one of its most striking illustrations—the fact that the actual outcome of two-person bargaining depends significantly on social conventions.

More importantly, the analysis of higgling, in revealing the inadequacies of the customary conception of market transactions, demonstrates that institutions are but one of the influences to be acknowledged to enrich the concept of *homo economicus.*

Conclusion

Once the role of social conventions in determining exchange outcomes is acknowledged, the psychological dimension of transactions remains to be elucidated. Rutherford recalls that Commons rejected the assumption of homogeneous agents and stressed the importance of personality and differential negotiational ability of transactors (p. 270). Jevons himself claimed that "the result of the bargain will greatly depend upon the comparative amount of knowledge of each other's position and needs which either bargainer may possess . . . the art of bargaining" (Morgan, pp. 243-244n). These examples suggest that the question as to how economic agents come to know about each other's characteristics should be given more weight in economic analysis. Social psychology and anthropology have opened the way: one way to acquire knowledge about others is to empathise with them, that is, to imagine what goes on inside their heads and consequently be able to see things from their perspective. This implies that it is difficult to study higgling without changing our view of *homo economicus*, so that the latter "be in possession of some apparatus for estimating the *inclinations* of others" (Binmore 1994, p. 57).

In sum, in accounting for the exclusion of higgling from the discipline by the fact that equilibrium has long been assumed rather than explained, this book also emphasizes the limits today's economists face when rediscovering and examining issues that have been excluded from economics as the result of its emancipation from other disciplines.

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